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2008 MAY 30 P 3: 11

SUPREME COURT OF THE STATE OF WASHINGTON

80450-8

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CLERK OF SUPREME COURT
STATE OF WASHINGTON

CHADWICK FARMS OWNERS ASSOCIATION,
a Washington nonprofit corporation, ERK

Respondent,

v.

FHC, LLC, a Washington limited liability company,

Petitioner,

v.

AMERICA 1ST ROOFING & BUILDERS, INC., a Washington corporation; CASCADE UTILITIES, INC., a Washington corporation; MILBRANDT ARCHITECTS, INC., P.S., a Washington corporation; PIERONI ENTERPRISE, INC., d/b/a PIERONI'S LANDSCAPE CONSTRUCTION, a Washington corporation, TIGHT IS RIGHT CONSTRUCTION, a Washington corporation; GUTTER KING, INC., a Washington corporation,

Respondents.

SUPPLEMENTAL BRIEF OF PETITIONER FHC, LLC

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I. IDENTITY OF PETITIONER

The Petitioner is FHC, LLC, a cancelled LLC, and Defendant and Respondent/Cross-Appellant below.

II. DECISION

On June 18, 2007 the Washington State Court of Appeals issued its decision, affirming in part and reversing in part, the September 30, 2005 summary judgment dismissal of all claims by the trial court. *Chadwick Farms Owners Assn. v. FHC, LLC*, 139 Wash.App. 300, 160 P.3d 1061 (2007). The Court of Appeals reversed the dismissal of Respondent Chadwick Farms Homeowners Association's ("HOA") claims against FHC, LLC ("FHC") and affirmed the dismissal of FHC's third-party claims against Respondent subcontractors.

III. ISSUES PRESENTED FOR REVIEW

1. Did the Court of Appeals err in failing to affirm dismissal of suit against FHC, a cancelled LLC, pursuant to RCW.25.15.070 and RCW 25.15.080?
2. Did the Court of Appeals err when it chose to rewrite RCW 25.15.303 because of what it characterized as an "inartful" word choice by the Legislature?

3. Did the Court of Appeals err when it restricted the RCW 25.15.270 winding up period to two years following administrative dissolution?
4. Did the Court of Appeals err when it held that RCW 25.15.303, a June 2006 LLC Act statutory amendment, applied retroactively?
5. Did the Court of Appeals err in affirming the dismissal of FHC's third party claims against its subcontractors?

IV. STATEMENT OF THE CASE

A. Factual Background.

FHC was formed on December 23, 1999 as a limited liability company ("LLC") for the purpose of constructing the Chadwick Farms project ("Project"). CP 76. Following construction of the Project, FHC ceased active operations. CP 76. On March 24, 2003, FHC was administratively dissolved by the Secretary of State. CP 13. On March 24, 2005, FHC's Certificate of Formation was cancelled pursuant to RCW 25.15.290(4), and FHC ceased existence as a legal entity.

B. Procedural Background.

On August 18, 2004, the HOA brought a claim for construction defects against FHC. CP 15-19. On May 11, 2005, after completing its forensic investigation, FHC filed a third-party complaint against the

subcontractors and design professionals implicated by the HOA's allegations. CP 139-152. On August 24, 2005, FHC moved for summary judgment dismissal of the HOA's claims on the ground that FHC ceased to exist because of the March 24, 2005 cancellation and that all claims against it abated. CP 1-19. Third-party defendants moved for summary judgment dismissal of FHC's third-party claim arguing that FHC could not pursue claims as a legal non-entity. CP 20-51. On September 30, 2005, the trial court entered an order dismissing with prejudice the HOA's complaint against FHC and FHC's third-party complaint. CP 98-101; 102-112.

C. Decision by the Court of Appeals.

The Court of Appeals held that RCW 25.15.303, a 2006 amendment to the LLC Act providing a three-year survival period to commence actions against a dissolved LLC, applied retroactively, and reinstated the suit by HOA against FHC. The Court further held that the survival amendment only preserved actions against an LLC and not actions brought by an LLC. Thus, FHC lacked standing to prosecute its claims against subcontractors.

The Court of Appeals interpreted RCW 25.15.285 to mean that an administratively cancelled LLC has only two years to complete winding up activities after dissolution, including active litigation. Notwithstanding

there is no provision to reinstate a cancelled LLC, it ruled that FHC had to reinstate itself in order to continue its third-party claims.

The Court of Appeals reversed the trial court's dismissal of claims against FHC, retroactively applying RCW 25.15.303. On June 7, 2006, while the appeal was pending, RCW 25.15.303 was added to the Washington LLC Act. RCW 25.15.303 creates a three-year survival of claims period after an LLC is dissolved. It makes no reference to and takes no account of LLC statutory cancellation provisions. Despite the express amendment language limiting the application of RCW 25.15.303 to dissolved LLCs, the Court of Appeals chose to "rewrite" the statute because of what it characterized as an "inartful" word choice by the legislature, i.e., selecting dissolution rather than cancellation as the commencement of the 3 year survival period. It ruled that the three-year survival period applied even after an LLC has been cancelled.

V. ARGUMENT

A. The New Survival of Claims Amendment Was Wrongly Applied to FHC, LLC, a cancelled LLC.

The legal status of LLCs in Washington is governed by the LLC Act. Formation of an LLC occurs when a Certificate of Formation ("Certificate") is executed and filed with the Secretary of State. RCW 25.15.070. Termination of an LLC is often a two-step process: (1)

dissolution of an LLC and (2) cancellation of the Certificate. Once the LLC's Certificate is cancelled, the LLC ceases to exist for all purposes. RCW 25.15.270(2)(c). Dissolution of FHC was by Secretary of State administrative action on March 24, 2003 for failing to file its annual report. RCW 25.15.280.

A dissolved LLC continues to exist for purposes of winding up.

See RCW 25.15.285(3) and RCW 25.15.290. RCW 25.15.295(2) reads:

Upon dissolution of a limited liability company and *until the filing of a certificate of cancellation as provided in RCW 25.15.080*, the persons winding up the limited liability company's affairs may, in the name of, and for and on behalf of, the limited liability company, prosecute and defend suits, whether civil, criminal, or administrative, gradually settle and close the limited liability company's business, dispose of and convey the limited liability company's property, discharge or make reasonable provision for the limited liability company's liabilities, and distribute to the members any remaining assets of the limited liability company.

RCW 25.15.295. RCW 25.15.080 reads:

A certificate of formation shall be canceled upon the effective date of the Certificate of Cancellation, or as provided in RCW 25.15.290, or upon the filing of articles of merger if the limited liability company is not the surviving or resulting entity in a merger . . .

RCW 25.15.080 (*emphasis added*). RCW 25.15.290(4) reads:

If an application for reinstatement is not made within the two-year period set forth in subsection (1) of this section, or if the application made within this period is not granted,

the Secretary of State shall cancel the limited liability company's Certificate of Formation.

RCW 25.15.290(4) (*emphasis added*).

FHC's Certificate was cancelled on March 24, 2003 and FHC ceased to exist as a separate legal entity:

A limited liability company formed under this chapter shall be a separate legal entity, **the existence of which as a separate legal entity shall continue until cancellation of the limited liability company's Certificate of Formation.**

RCW 25.15.070(2)(c) (*emphasis added*). Once FHC's Certificate was cancelled, the HOA's suit against FHC abated as there is no basis permitting claims to continue against a cancelled LLC, a legal non-entity. There is also no statutory basis to extend the life of an LLC once its Certificate is cancelled.

It is the golden rule of statutory interpretation that unreasonable results be rejected. *See Cooper's Mobile Homes, Inc. v. Simmons*, 94 Wash.2d 321, 333, 617 P.2d 415, 422 (1980)¹. The express provision of RCW 25.15.295(2) states that suit can be maintained against an LLC only until it is cancelled pursuant to RCW 25.15.080. Once FHC was

¹ The "golden rule" of statutory interpretation mandates - "(The) unreasonableness of the result produced by one among alternative possible interpretations of a statute is a reason for rejecting that interpretation in favor of another which would produce a reasonable result." *Id.*

cancelled, it ceased to exist as a legal entity for all purposes. Permitting suit against a cancelled LLC is an unreasonable result.

During the post-dissolution process an LLC continues to exist, but its activities are limited to the winding-up activities set forth in RCW 25.15.295(2), which includes prosecuting and defending claims. RCW 25.15.295. Under the LLC Act, there is a difference between “dissolution” of an LLC and the “cancellation of its certificate of formation.” Once an LLC’s Certificate is cancelled, it no longer exists for any purpose. 25.15.070(2)(c). Because it ceased to exist, the HOA’s claims against FHC should be dismissed. The survival amendment keyed to dissolution simply does not apply to a cancelled LLC.

The Legislature chose not to create a survival of claims provision that would apply to cancelled LLCs. The Legislature left intact the termination of an LLC upon cancellation of its Certificate. Thus, the Court of Appeals had no statutory basis to resurrect its status as a legal entity amenable to suit. Disregarding the plain meaning and legal effect of RCW 25.15.070(2)(c), the Court of Appeals rendered that statutory provision meaningless in contravention of the principle that a court may not construe a statute in a way that renders statutory language meaningless or superfluous. *Lakemont Ridge Homeowners Association v. Lakemont Ridge Limited P'ship*, 156 Wn.2d 696, 698-99, 131 P.3d 905 (2006). The

Court of Appeals reiterated this axiom in its decision construing the Model Business Act, Title 23B RCW. *Ballard Square Condominium Owners Assn. v. Dynasty Construction Co.*, 126 Wn. App. 285, 291-92 n.22, 108 P.3d 818 (2005). The Court of Appeals refused to follow its own precedent, disregarding the cancellation provision in the LLC Act. This Court also applied the principle of not rendering statutory language meaningless or superfluous in its *Ballard Square* decision. *Ballard Square Condominium Owners Assn. v. Dynasty Construction Co.*, 158 Wn.2d 603, 610, 146 P.3d 914 (2006). The LLC Act terminates the existence of a LLC upon cancellation and does not distinguish between claims that were brought prior to cancellation or those brought after cancellation.

It is also a basic principle of statutory interpretation that a Court cannot add words to a statutory provision that are not there. *See Restaurant Development, Inc. v. Cananwill, Inc.*, 150 Wash.2d 674, 681, 80 P.3d 598, 601-02 (2003). RCW 25.15.295 is clear. Once an LLC is cancelled, it is no longer a legal entity and persons winding up an LLC's affairs may not "prosecute and defend suits". To find an exception for claims preserved for three years following dissolution would be to add words to the statute that do not exist. The Court of Appeals effectively

substituted the word “cancellation” for “dissolution” in violation of this principle.

While the appeal was pending, the Legislature passed RCW 25.15.303 creating a three year survival of claims after date of LLC dissolution. The Court of Appeals held that the new statute applied retroactively and to cancelled LLCs. It added “cancellation” to the amendment. RCW 25.15.303 provides for a survival of claims period only against dissolved LLCs similar to survival periods contemporaneously created by the 2006 Legislature for dissolved corporations under the Business Corporation Act. *See* RCW 23B.14.340. The relevant language of RCW 25.15.303 reads:

The dissolution of a limited liability company does not take away or impair any remedy available against that limited liability company.... (emphasis added).

No amendment was made to affect the cancellation sections of the LLC statute. The amendment left RCW 25.15.070(2)(c) fully intact. The Court of Appeals exceeded its authority by effectively rewriting the statute to substitute “cancelled” for “dissolved” because of what it perceived to be “inartful” word choice by the Legislature in its reference point for the survival of claims.² A Court may not rewrite a statute merely because it

² The Court’s ruling that suit may be brought within three years of dissolution albeit after an LLC cancellation begs the question of how a successful plaintiff might collect a

could have been drafted more clearly. *State v. Freeman*, 124 Wn.App. 413, 415, 101 P.3d 878 (2004). RCW 25.15.303 on its face only authorizes actions against a “dissolved” LLC and does not allow claims against an LLC after cancellation.

B. The Court of Appeals Erred When it Held that RCW 25.15.303 Applied Retroactively to Cancelled LLCs.

The Court of Appeals erred when it found RCW 25.15.303 applied retroactively. Statutory amendments are generally prospective but can act retroactively if the legislation reflects that intention or if the amendment is curative or remedial. *1000 Virginia Ltd. Partnership v. Vertecs*, 158 Wn.2d 566, 584, 146 P.3d 423 (2006). The Court of Appeals erroneously adopted the retroactivity analysis of this Court in *Ballard Square Condominium Owners Association v. Dynasty Construction Co.*, 158 Wn.2d 603, 146 P.3d 914 (2006). In its *Ballard Square* decision, this Court set forth the general rule that, as to pre-existing causes of action, a new limitations period runs from the date of its enactment. *Ballard Square*, 158 Wn.2d at 616. There is a qualifier to the general rule:

“[T]he limitation of the new statute, as applied to pre-existing causes of action, commences when the action is first subjected to the operation of the statute, *unless the Legislature has otherwise provided.*” (Internal citations omitted.) *Id.*

judgment against a legal non-entity. A judgment can only be entered against a legal person or a legal entity. Any judgment against FHC would be unenforceable.

If this rule is applied, there is no survival action available to the HOA for its claims against FHC because they were brought before June 6, 2006, the date of the amendment. No new limitations period commenced.

In *Ballard Square*, the Court found clear evidence that a survival of claims amendment, also added to the Model Business Act in June 2006 at RCW 23B.14.340, "otherwise provided". Therein, the Legislature expressed its clear intention to apply the survival of claim amendment retroactively by creating two periods for survival of claims: a two year limitation period for corporations that dissolved before the amendment's effective date and three-year period for corporation dissolutions after the amendment. *Id.* at 616. The statute showed clear legislative intent that it applied to actions arising before its effective date. *Id.*

Here, the Legislature created a single 3-year survival period for claims against dissolved LLCs. Both the survival amendments to the Model Business Act and the amendments to the LLC Act were enacted by the same Legislature in the same sessions. Had the Legislature intended a retroactive effect of the LLC survival statute, it certainly knew how to make its intentions plain as it did when it amended the Corporate Business Act. Lacking clear legislative intent, there is no retroactivity.

In *1000 Virginia Limited Partnership v. Vertecs Corporation*, 158 Wn.2d 566, 584, 146 P.3d 423 (2006), this Court made its most recent

pronouncement concerning retroactive application of statutory amendments. The Court reiterated the axiom that a statute may be retroactively applied if the Legislature so intends and where retroactive application does not impair a constitutional right. *Id.* A statute may also apply retroactively if it is curative or remedial. *Id.* An enactment is curative only if it clarifies or technically corrects an ambiguous statute. *McGee Guest Homes*, 142 Wn.2d at 325, 12 P.3d 144 (2000). RCW 25.15.303 does not clarify any statute. It creates a new survival period for claims against a dissolved LLC which never existed before.

A statute is remedial when it relates to practice, procedure, or remedies and does not affect a substantive or vested right. *1000 Virginia Limited Partnership* at 586-87. RCW 25.15.303 does not supplement an existing right or remedy. Instead, it grants a new substantive right to bring claims against a dissolved LLC. Washington Courts consistently refuse to apply a statute retroactively if it brings about a change in substantive rights and imposes new liability on defendants. *Bayless v. Community College Dist. No. XIX*, 84 Wn.App. 309, 312, 927 P.2d 254 (1996).

The Court is urged to follow its result in *1000 Virginia*, where it held that RCW 4.16.326(1)(g), a statutory amendment, did not apply retroactively. *1000 Virginia*, 158 Wn.2d at 587. In *1000 Virginia*, the Court found no basis for departing from the general rule that newly-enacted

statutes and amendments to statutes apply prospectively. See *Ballard Square*, 158 Wn.2d at 618. In its *Ballard Square* analysis, the Court distinguished the statutory amendment in *1000 Virginia* from the statutory amendment in *Ballard Square* by looking at the face of the amendments themselves. *Id.* The Court found that RCW 23B.14.340, the survival of action amendment to the corporate statute, on its face showed clear legislative intent that the statute apply retroactively. The language of the amendment in *1000 Virginia* did not have any indication on its face that it was to be retroactive. Here there is also no basis to depart from the general rule that newly-enacted statutes and amendments apply prospectively. There is no indication on the face of the amendment that the Legislature intended retroactivity. The fact that the Legislature did not enact a bifurcated survival of claims scheme against LLCs as it did with the corporation amendment answers the question of intention. The amendment is prospective because it did not “otherwise indicate.”

C. The Court of Appeals Erred When It Determined the LLC Act Has A Two-Year Time Limit to Complete Winding Up.

Another legal question before the Court of Appeals was whether FHC had the capacity to sue or be sued after it was administratively cancelled in March 2005 as part of ongoing “winding up” activities. The

legal issue is whether an LLC after its Certificate is cancelled can continue to wind up. RCW 25.15.295(2).

The statutes applicable to dissolution, winding up and cancellation are difficult to reconcile, especially in the context of administratively dissolved LLCs. However, each provision must be given weight. RCW 25.15.295 permits a dissolved LLC to wind up, including prosecuting and defending claims, until a Certificate of Cancellation is filed. An LLC itself can only file a Certificate of Cancellation once it completes winding up, including making provisions for known or contingent claims. RCW 25.15.300. An administratively dissolved LLC continues its existence as a legal entity even as it winds up. RCW 25.15.285.

A Certificate of LLC Formation is automatically cancelled by the Secretary of State after two years of dissolution. One issue on appeal was whether an administratively dissolved and cancelled LLC in the midst of ongoing litigation continues to exist solely for purposes of winding up that litigation. The court incongruently both allowed and refused a cancelled LLC to continue litigation once cancellation occurred.

RCW 25.15.270 entitled "Dissolution" lists six events that affect an LLC dissolution and provides the only activities an LLC can perform are those necessary to winding up. However, because of a poor word phrasing in the statute, the statute can be read that upon an event of

dissolution, winding up is also complete. The Court of Appeals made that unreasonable interpretation. The statute provides:

A limited liability company is dissolved and its affairs **shall be wound up** upon the first to occur of the following:

(1)(a) The dissolution date, if any, specified in the certificate of formation. If a dissolution date is not specified in the certificate of formation, the limited liability company's existence will continue until the first to occur of the events described in subsections (2) through (6) of this section. If a dissolution date is specified in the certificate of formation, the certificate of formation may be amended and the existence of the limited liability company may be extended by vote of all the members;

(b) This subsection does not apply to a limited liability company formed under RCW 30.08.025 or 32.08.025.

(2) The happening of events specified in a limited liability company agreement;

(3) The written consent of all members;

(4) Unless the limited liability company agreement provides otherwise, ninety days following an event of dissociation of the last remaining member, unless those having the rights of assignees in the limited liability company under RCW 25.15.130(1) have, by the ninetieth day, voted to admit one or more members, voting as though they were members, and in the manner set forth in RCW 25.15.120(1);

(5) The entry of a decree of judicial dissolution under RCW 25.15.275; or

(6) The expiration of two years after the effective date of dissolution under RCW 25.15.285 without the reinstatement of the limited liability company.

RCW 25.15.270 (emphasis added).

The prefatory language of RCW 25.15.270 uses the phrase “shall be wound up”. According to the Court of Appeals, any of one of the six events terminates winding up, presumably in the middle of an ongoing litigation, as here. When the statute is given a more reasonable interpretation the happening of one of the six events was solely meant to *trigger* winding up, not terminate winding up. By limiting its focus, the Court of Appeals found that there was an arbitrary two-year time limitation to complete winding up for administratively cancelled LLCs. This ruling essentially renders meaningless the other winding up provisions in the LLC Act. As interpreted by the Court of Appeals, the Act now arbitrarily terminates the winding up period upon dissolution regardless of whether winding up is actually completed.

Because more than two years passed since FHC was administratively dissolved, its winding up period according to the Court of Appeals terminated, and FHC did not have standing to prosecute claims against the subcontractors.

D. The LLC Statute Is Not Analogous To the Business Corporation Act, Chapter 23B-14 RCW.

When the Legislature amended the Business Corporation Act to provide survival periods for claims against dissolved business corporations, the reference to date of dissolution as the key event was clear and

unambiguous. A corporation was amenable to suit as a legal entity for three or two years following dissolution. The Business Corporation Act has no provision for canceling a corporation making it a legal non-entity. A corporation does not become a legal non-entity after a two-year dissolution period like an LLC. The LLC Act provides:

A limited liability company formed under this chapter shall be a separate legal entity, the existence of which as a separate legal entity shall continue until cancellation of the limited liability company certificate of formation. (Emphasis added.). RCW 25.15.070(2)(c).

The Court of Appeals failed to reconcile and give meaning and weight to the cancellation section in the LLC statute. All statutory provisions must be given equal weight. The Court of Appeals agreed that prior to the 2006 amendment there was no survival of an action or claim against a cancelled LLC. However, it believed the amendment somehow reinstated a claim against a cancelled LLC. The 2006 amendment, however, made no changes to the LLC's status as a legal non-entity upon cancellation pursuant to RCW 25.15.070. As inartful as the Legislature may have been in amending the LLC statute in 2006, all statutory provisions must be reconciled.

The only reasonable interpretation of the LLC statute, as amended, is that there is a three-year survival claim following date of dissolution but only if the LLC has not been canceled. The Court of Appeals decision gave effect

to the three-year survival of claims provision based on date of dissolution but eviscerated the cancellation (and winding up) statutory provisions.

The Court of Appeals ruled that the survival provision at issue applies to dissolved LLCs whether or not a certificate of cancellation was issued because it believed it would render the 2006 amendments inoperative as it “would link the survival of claims not to a specific survival period, but rather to the actions or, as in this case, non-action of a company.” The Court of Appeals failed to realize that the 2006 amendment is not inoperative in all circumstances. In the absence of a cancellation, the three-year survival statute would operate to create a survival of claims period tied to dissolution.

FHC was cancelled by the Secretary of State. It became a legal non-entity and the claims against it then lost legal force, regardless of the 2006 amendment. If claims against it can legally continue, so also should its third-party claims. If FHC survived cancellation, it had the right to wind up, including prosecution and defense of suits. The Court of Appeals believed it was the non-action of FHC that resulted in cancellation. However, FHC was vigorously defending itself and pursuing third-party action to recover any liabilities it may have had to the HOA.

E. The Court of Appeals Erred in Dismissing FHC, LLC's Claims Against Subcontractors.

During the period of administrative dissolution, FHC was defending itself against the HOA's claims and investigating potential third-party claims. Albeit after cancellation, but arguably in the course of a winding up the litigation that commenced prior to cancellation, FHC asserted its third-party claims. It either was or was not a legal entity for the purpose of being a party to the litigation. The Court of Appeals improperly delimited the winding up period to two years, holding that FHC could only pursue third-party claims if it reinstated itself. Its interpretation is contrary to the language of the LLC Act which was not affected by the 2006 amendment. If FHC was in the process of winding up, it could not itself file a certificate of cancellation without violating the Act. The Court erroneously ruled that FHC had to reinstate itself as an active corporation to pursue third-party claims, but was open to HOA litigation even if it failed to reinstate. A cancelled LLC has no means to reinstate its certificate of formation. There is nothing in RCW 25.15.303 that anticipates that an LLC must respond to legal action after its Certificate is cancelled.

On the one hand the Court of Appeals erroneously disregarded FHC's cancellation making it a non-entity subject to suit. On the other hand, it ruled it had no standing as a legal entity to pursue third-party claims.

Either FHC is shielded from and cannot pursue claims upon cancellation or it survives and has the right to pursue claims after cancellation as a continuation of winding up. The LLC framework arguably allows for a winding up process notwithstanding dissolution or cancellation administratively. Cancellation of the Certificate means the LLC can no longer actively perform its regular business, but it does not preclude winding up.

VI. CONCLUSION

Notwithstanding the creation of a survival of claims provision, the Legislature left intact the LLC cancellation provisions. The legal effect of cancellation cannot be ignored. The LLC survival amendment is prospective in application under well established law and precedent. FHC was not amenable to suit. Alternatively, the proper way to resolve the legislative intent is to allow a cancelled LLC to defend and bring claims as part of a winding up process.

Respectfully submitted this 30th day of May, 2008.

FORSBERG & UMLAUF, P.S.

By 

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CERTIFICATE OF SERVICE

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STATE OF WASHINGTON

2008 MAY 30 P 3:11

BY RONALD R. CARPENTER

CLERK

The undersigned certifies under the penalty of perjury under the laws of the State of Washington that I am now and at all times herein mentioned, a citizen of the United States, a resident of the State of Washington, over the age of eighteen years, not a party to or interested in the above-entitled action, and competent to be a witness herein.

On the date given below I caused to be served the foregoing FHC, LLC'S PETITION FOR REVIEW on the following individuals in the manner indicated:

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SIGNED this 30th day of May, 2008, at Seattle, Washington.


Elizabeth Mullen